An FTC Guide to Mergers

Markets

THE LAW BARS MERGERS THAT HAVE POTENTIAL HARMFUL EFFECTS in a “line of commerce” in a “section of the country.” In practical terms, this means the agency will examine the businesses of the merging parties both in terms of what they sell (a product dimension) and where they sell it (a geographic dimension).

MARKET ANALYSIS STARTS with the products or services of the two merging companies. In the case of a horizontal merger, the companies have products or services that customers see as close substitutes. Before the merger, the two companies may have offered customers lower prices or better service to gain sales from one another. After the merger, that beneficial competition will be gone as the merged firm will make business decisions regarding the products or services of both companies. The loss of competition may not matter if a sufficient number of customers are likely to switch to products or services sold by other companies if the merged company tried to increase its prices. In that case, customers view the products of other rivals to be good substitutes for the products of the merging firms and the merger may not affect adversely the competitive process with higher prices, lower quality, or reduced innovation if there is a sufficient number of competitive choices after the deal.

In the most general terms, a product market in an antitrust investigation consists of all goods or services that buyers view as close substitutes. That means if the price of one product goes up, and in response consumers switch to buying a different product so that the price increase is not profitable, those two products may be in the same product market because consumers will substitute those products based on changes in relative prices. But if the price goes up and consumers do not switch to different products, then other products may not be in the product market for purposes of assessing a merger’s effect on competition.

In some investigations, the agencies are able to explore customers’ product preferences using actual prices and sales data. For instance, when the FTC challenged the merger of Staples and Office Depot, the court relied on pricing data to conclude that consumers preferred to shop at an office superstore to buy a wide variety of supplies, even though those same products could be purchased at a combination of different retailers. The product market in that case was the retail sale of office supplies by office supply superstores. In the majority of cases, however, the agency relies on other types of evidence, obtained primarily from customers and from business documents. For instance, evidence that customers highly value certain product attributes may limit their willingness to substitute other products in the event of a price increase. In the FTC’s review of a merger between two ready-mix concrete suppliers, customers believed that asphalt and other building materials were not good substitutes for ready-mix concrete, which is pliable when freshly mixed and has superior strength and permanence after it hardens. Based on this and other evidence, the product market was limited to ready-mix concrete.

A geographic market in an antitrust investigation is that area where customers would likely turn to

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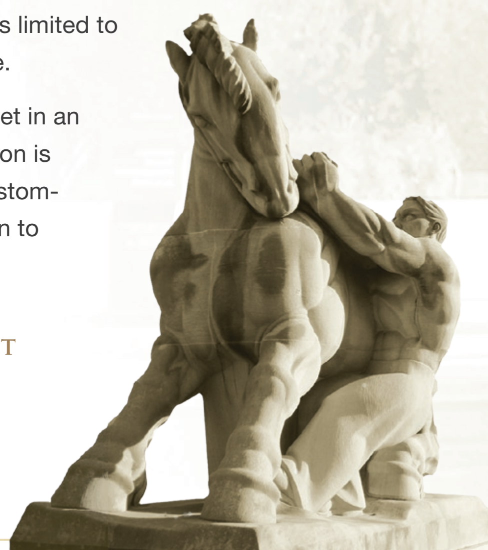

buy the goods or services in the product market. Competition may be limited to a small area because of the time or expense involved in buying a lower-cost product elsewhere. For instance, in a merger between two companies providing outpatient dialysis services, the FTC found that most patients were willing to travel no more than 30 miles or 30 minutes to receive kidney dialysis treatment. The FTC identified 35 local geographic markets in which to examine the effects of that merger. The FTC often examines local geographic markets when reviewing mergers in retail markets, such as supermarkets, pharmacies, or funeral homes, or in service markets, such as health care.

Shipping patterns are often a primary factor in determining the scope of a geographic market for intermediate or finished goods. In some industries, companies can ship products worldwide from a single manufacturing facility. For other products where service is an important element of competition or transportation costs are high compared with the value of the product, markets are more localized, perhaps a country or region of the country. For example, when examining the market for industrial gases, the FTC found that the cost of transporting liquid oxygen and liquid nitrogen limited customers to sources within 150 to 200 miles of their business.